

The penalty for failure to disclose information with respect to a reportable transaction is in addition to any accuracy-related penalty that may be imposed on the taxpayer.

#### EFFECTIVE DATE

The provision applies to transactions entered into after date of enactment.

#### 6. Registration of certain tax shelters offered to non-corporate participants (sec. 206)

##### PRESENT LAW

A promoter of a confidential corporate tax shelter is required to register the tax shelter with the IRS (sec. 6111(d)). Registration is required not later than the next business day after the day when the tax shelter is first offered to potential users. For this purpose, a confidential corporate tax shelter includes any entity, plan, arrangement or transaction (1) a significant purpose of which is the avoidance or evasion of Federal income tax for a direct or indirect participant that is a corporation, (2) that is offered to any potential participant under conditions of confidentiality, and (3) for which the tax shelter promoters may receive aggregate fees in excess of \$100,000.

The penalty for failing to timely register a confidential corporate tax shelter is the greater of \$10,000 or 50 percent of the fees payable to any promoter with respect to offerings prior to the date of late registration unless due to reasonable cause (sec. 6707(a)(3)). Intentional disregard of the requirement to register increases the 50-percent penalty to 75 percent of the applicable fees.

#### EXPLANATION OF PROVISION

The bill deletes the requirement that a direct or indirect participant must be a corporation. Thus, the provision extends the present-law registration requirements to include a promoter of any confidential tax shelter (regardless of the participant). The penalty for failing to timely register a confidential tax shelter remains unchanged (i.e., the greater of \$10,000 or 50 percent of the fees payable to any promoter with respect to offerings prior to the date of late registration).

#### EFFECTIVE DATE

The provision applies to any tax shelter interest that is offered to potential participants after the date of enactment.

#### TITLE III—LIMITATIONS ON IMPORTATION AND TRANSFER OF BUILT-IN LOSSES

##### 1. Limitation on importation of built-in losses (sec. 301)

##### PRESENT LAW

Under present law, the basis of property received by a corporation in a tax-free incorporation, reorganization, or liquidation of a subsidiary corporation is the same as the adjusted basis in the hands of the transferor, adjusted for gain or loss recognized by the transferor (Secs. 334(b) and 362(a) and (b)). If a person or entity that is not subject to U.S. income tax transfers property with an adjusted basis higher than its fair market value to a corporation that is subject to U.S. income tax, the "built-in" loss would be imported into the U.S. tax system, and the transferee corporation would be able to recognize the loss in computing its U.S. income tax.

#### EXPLANATION OF PROVISION

The bill provides that if a net built-in loss is imported into the U.S. in a tax-free organization or reorganization from persons not subject to U.S. tax, the basis of all properties so transferred will be their fair market value. A similar rule will apply in the case of the tax-free liquidation by a domestic corporation of its foreign subsidiary.

Under the bill, a net built-in loss is considered imported into the U.S. if the aggregate

adjusted bases of property received by a transferee corporation subject to U.S. tax from persons not subject to U.S. tax with respect to the property exceeds the fair market value of the properties transferred. Thus, for example, if in a tax-free incorporation, some properties are received by a corporation from U.S. persons, and some properties are relieved from foreign persons not subject to U.S. tax, this provision applies to the aggregate properties relieved from the foreign persons. In the case of a transfer by a partnership (either domestic or foreign), this provision applies as if the properties had been transferred by each of the partners in proportion to their interests in the partnership.

#### EFFECTIVE DATE

The provision applies to transactions after the date of enactment.

##### 2. Disallowance of partnership loss transfers (sec. 302)

##### PRESENT LAW

##### Contributions of property

Under present law, if a partner contributes property to a partnership, generally no gain or loss is recognized to the contributing partner at the time of contribution (Sec. 721). The partnership takes the property at an adjusted basis equal to the contributing partner's adjusted basis in the property (Sec. 723). The contributing partner increases its basis in its partnership interest by the adjusted basis of the contributed property (Sec. 722). Any items of partnership income, gain, loss and deduction with respect to the contributed property is allocated among the partners to take into account any built-in gain or loss at the time of the contribution (Sec. 704(c)(1)(A)). This rule is intended to prevent the transfer of built-in gain or loss from the contributing partner to the other partners by generally allocating items to the noncontributing partners based on the value of their contributions and by allocating to the contributing partner the remainder of each item. (Note: where there is an insufficient amount of an item to allocate to the noncontributing partners, Treasury regulations allow for reasonable allocations to remedy this insufficiency. Treas. Reg. sec. 1-704(c) and (d)).

If the contributing partner transfer its partnership interest, the built-in gain or loss will be allocated to the transferee partner as it would have been allocated to the contributing partner (Treas. Reg. sec. 1.704-3(a)(7)). If the contributing partner's interest is liquidated, there is no specific guidance preventing the allocation of the built-in loss to the remaining partners. Thus, it appears that losses can be "transferred" to other partners where the contributing partner no longer remains a partner.

##### Transfers of partnership interests

Under present law, a partnership does not adjust the basis of partnership property following the transfer of a partnership interest unless the partnership has made a one-time election under section 754 to make basis adjustments (Sec. 743(a)). If an election is in effect, adjustments are made with respect to the transferee partner in order to account for the difference between the transferee partner's proportionate share of the adjusted basis of the partnership property and the transferee's basis in its partnership interest (Sec. 743(b)). These adjustments are intended to adjust the basis of partnership property to approximate the result of a direct purchase of the property by the transferee partner. Under these rules, if a partner purchases an interest in a partnership with an existing built-in loss and no election under section 754 in effect, the transferee partner may be allocated a share of the loss when the partnership disposes of the property (or depreciates the property).

##### Distributions of partnership property

With certain exceptions, partners may receive distributions of partnership property without recognition of gain or loss by either the partner or the partnership (Sec. 731 (a) and (b)). In the case of a distribution in liquidation of a partner's interest, the basis of the property distributed in the liquidation is equal to the partner's adjusted basis in its partnership interest (reduced by any money distributed in the transaction) (Sec. 732(b)). In a distribution other than in liquidation of a partner's interest, the distributee partner's basis in the distributed property is equal to the partnership's adjusted basis in the property immediately before the distribution, but not to exceed the partner's adjusted basis in the partnership interest (reduced by any money distributed in the same transaction) (Sec. 734(a)).

Adjustments to the basis of the partnership's undistributed properties are not required unless the partnership has made the election under section 754 to make basis adjustments (sec. 734(a)). If an election is in effect under section 754, adjustments are made by a partnership to increase or decrease the remaining partnership assets to reflect any increase or decrease in the adjusted basis of the distributed properties in the hands of the distributee partner (Sec. 734(b)). To the extent the adjusted basis of the distributed properties increases (or loss is recognized) the partnership's adjusted basis in its properties is decreased by a like amount; likewise, to the extent the adjusted basis of the distributed properties decrease (or gain is recognized), the partnership's adjusted basis in its properties is increased by a like amount. Under these rules, a partnership with no election in effect under section 754 may distribute property with an adjusted basis lower than the distributee partner's proportionate share of the adjusted basis of all partnership property and leave the remaining partners with a smaller net built-in gain or a larger net built-in loss than before the distribution.

#### DESCRIPTION OF PROVISION

##### Contributions of property

Under the bill, a built-in loss may be taken into account only by the contributing partner and not by other partners. Except as provided in regulations, in determining the amount of items allocated to partners other than the contributing partner, the basis of the contributed property shall be treated as the fair market value on the date of contribution. Thus, if the contributing partner's partnership interest is transferred or liquidated, the partnership's adjusted basis in the property will be based on its fair market value at the date of contribution, and the built-in loss will be eliminated. (Note: it is intended that a corporation succeeding to attributes of the contributing corporate partner under section 381 shall be treated in the same manner as the contributing partner).

##### Transfers of partnership interests

The bill provides that the basis adjustment rules under section 743 will be required in the case of the transfer of a partnership interest with respect to which there is a substantial built-in loss. For this purpose, a substantial built-in loss exists where the transferee partner's proportionate share of the adjusted basis of the partnership property exceeds 110 percent of the transferee partner's basis in the partnership interest in the partnership. Thus, for example, assume that partner A sells his partnership interest to B for its fair market value of \$100. Also assume that B's proportionate share of the adjusted basis of the partnership assets is \$120. Under the bill, section 743(b) will apply and require a \$20 decrease in the adjusted basis of the partnership assets with respect to B, so that B